

PROTECTING YOUR D&O CONTRACT AGAINST RESCISSION

ISSUE

Protecting purchasers of D&O insurance against rescission by carriers is critical. By rescinding any policy of insurance, a carrier renders the entire contract void as if it had never existed. A carrier's right to rescind is typically based on the actions of the policyholder or its senior representatives during the process of applying for coverage (i.e., misrepresentations). This is a matter of particular relevance in D&O contracts where, although the policy is in the name of the corporation, the primary beneficiaries of coverage are actually a group of individuals (the directors and officers), many of whom will not be involved in the negotiation of the coverage.

IMPACT

Protection against rescission of a D&O policy comes in three main forms:

- 1. NEGOTIATING A SEVERABLE CONTRACT** In simple terms, individuals are only held accountable for their own actions or knowledge, and carriers have no recourse against them because of the actions of other insureds. This applies to both the application for coverage and the so-called misconduct exclusions. A properly drafted severability provision is the front line in defense against rescission. The key is in getting the right language, as no two carriers use the same severability endorsement, and many carriers have more than one endorsement of their own.

- 2. SIDE-A NON-RESCISSION** This is a specific provision by carriers that they cannot rescind coverage for non-indemnifiable loss (A-Side Claims) under any circumstances. This should now be a standard provision on all public D&O policies.
- 3. FULL NON-RESCISSION** An endorsement introduced by many carriers over the past 36 months that purports to render the entire policy non-rescindable. However, it often comes with a quid pro quo. The carriers waive their rights to rescind but typically exclude any claim based upon misrepresentations in the application for coverage.

Items 1 and 2 above are both pure benefits to a policyholder and should always be negotiated into the contract. The full non-rescission endorsement is a more complex matter. While it is inherently difficult for an insurer to maintain a successful rescission action, the imposition of such exclusions could weaken an insured's position. Although there is certainly a benefit to knowing that your policy cannot be rescinded for any reason, a well-crafted D&O contract should already contain adequate protection.

ACTION

- Ensure that all conduct-related elements of your D&O policy (application and exclusion provisions) provide the broadest protection available to you in the market. These elements are fundamental to the policy's performance and should be a key driver in the choice of carrier.



2. Ensure that the A-Side piece of your D&O policy cannot be rescinded under any circumstances.
3. Understand the pros and cons of buying a fully non-rescindable D&O contract. Discuss with your broker the rescission process and the protections afforded with and without this endorsement. Recognize the difference between a rescission action and a policy exclusion.
4. If you buy the non-rescindable coverage, understand what is excluded from your policy and the implications of the exclusion.

CONTACTS

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